

STATEMENT OF PETER KINZLER
ON BEHALF OF THE
COALITION FOR AUTO-INSURANCE REFORM
ON S. 837, THE AUTO CHOICE REFORM ACT OF 1999
BEFORE THE
COMMERCE, SCIENCE AND TRANSPORTATION COMMITTEE
UNITED STATES SENATE
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Summary of the Testimony of Peter Kinzler President, Coalition for Auto-Insurance Reform

The tort system provides inadequate compensation to injured persons, is too slow, pays too much money for fraud and lawsuits, and is too costly

- It has large compensation gaps, with 30% of all injured persons recovering nothing.
- People with minor economic losses recover, on average, far in excess of those losses, often by fraudulently inflating their claims.
- People with serious injuries recover, on average, less than half of their economic losses and nothing for pain and suffering, primarily because of the policy limits of other drivers' insurance.
- Payment of compensation for injuries is slow, often taking 2 to 3 years in major cities.
- Almost twice as many dollars are paid to lawyers as are paid to victims to compensate them for legitimate medical bills and lost wages.
- The system itself encourages massive fraud because pain and suffering awards are calculated as a multiple of medical expenses and lost wages.
- The system is too costly, because of the fraud and unnecessary attorneys' fees.

State experience with no-fault insurance identifies the path to a better auto insurance system

- 28 years of experience with 16 state laws has demonstrated that a primarily first party insurance system, where injured people are compensated for their losses by their own insurer without regard to fault, provides better compensation, in that it pays (1) *all* injured persons, (2) promptly, and (3) more in accord with the seriousness of their injuries.
- Some, but not all, of these laws have not worked to hold down costs because the restrictions on lawsuits for pain and suffering -- the trade-off for better compensation and lower premiums -- have been weakened by the trial bar. The creation and exploitation of loopholes by the opponents of reform are the major cause for unnecessarily high costs.

S. 837, the Auto Choice Reform Act of 1999, offers a prescription for lower premiums, better benefits and more consumer choice

- The new personal injury protection (PIP) system would:
 - fix the cost problems with state no-fault laws by eliminating the lawsuits for pain and suffering that encourage fraud and high costs.
 - let each motorist determine, for himself and his family, the appropriate balance between premiums and compensation in the event of an accident.
 - eliminate the compensation gaps of the tort system by paying *all* auto accident victims.
 - assure prompt payment for economic losses up to the level of people's policies. Prompt payment assures more complete and timely rehabilitation.
 - assure greater compensation for serious injuries, by combining first party benefits with the right to sue the other driver on a fault basis for any excess economic loss.
- If all people choose the new PIP system, annual savings will be \$35 billion. The savings are progressive, with poor people seeing the greatest percentage reductions.
- S. 837 gives people the option to stay in a fault-based system where they can recover both economic and non-economic damages. The cost would be about the same as today.

- S. 837 gives each State several options to prevent Auto Choice from becoming law there.

My name is Peter Kinzler. I am longtime advocate of automobile insurance reform¹ and President of the Coalition for Auto-Insurance Reform (CAR). CAR represents a cross-section of leading academics, insurers, consumer activists and business groups who support the adoption of legislation that would give motorists the opportunity to purchase insurance that would:

- * Pay medical, rehabilitation, wage loss and replacement services benefits, up to the limits of one's policy, to **all** insured automobile accident victims, and provide better coverage for more seriously injured persons.
- * Pay benefits within 30 days of submission of a bill or claim.
- * Lower automobile insurance premiums.

S. 837, the Auto Choice Reform Act of 1999, would give drivers throughout the United States the opportunity to purchase such insurance. It is legislation that would provide enormous benefits -- lower premiums, better compensation and more choice -- to American motorists.

WHY AMERICAN DRIVERS NEED AUTO INSURANCE REFORM: THE FAILURES OF THE TORT AND LIABILITY INSURANCE SYSTEM

Three times during the chairmanship of Warren Magnuson in the 1970s, the Senate Commerce Committee reported auto insurance reform bills to the Senate floor. Each time the legislation was reported by a wide bipartisan margin. Those bills would have set federal standards for no-fault automobile insurance. In 1974, the Senate passed one of those bills.

Despite the expansive nature of the Commerce Committee bill, in 1974, then-Governor Ronald Reagan expressed his frustration with state efforts to reform California's tort system for auto accidents and encouraged an effort to work with the sponsors of the federal standards reform bill.² Later in the decade, President Jimmy Carter endorsed the Senate bill and worked for its

¹My involvement with auto insurance reform dates back to the 1970s when I served as Counsel to the then-Consumer Protection and Finance Subcommittee of the House Commerce Committee. In that capacity, I worked on legislation that would have established federal standards for no-fault automobile insurance.

²In a March 14, 1974 letter, Governor Reagan wrote that "it would be far better if we could obtain legislation at the state level without having to have a federal standards bill. However, in this situation we are faced with two political realities with which we must deal. First is the likelihood that California will not enact no-fault legislation in the absence of a federal standards bill. Second, federal legislation may be enacted with or without our input. . . . It seems to me that if we oppose federal no-fault standards on principle, we will probably not have the opportunity to work with the sponsors to gain the kind of changes we would like to see. While the current proposed bill has gone a long way to eliminate the possibility of superimposing federal regulation of insurance on the state system, this is one of the areas where constructive criticism would probably be well received if it were offered by supporters in principle."

³In his 1979 State of the Union message, President Carter endorsed the federal standards

adoption.³ None of these bills became law.

Why was there broad support for passage of auto insurance reform legislation then and why should the Congress address the issue now? The answers lie in the ongoing deficiencies of the tort system and the lessons learned from more than 28 years of state experiments with different forms of no-fault insurance.

The seminal work on the deficiencies of the tort and liability insurance system in the 1970s was a 26-volume study completed by the U. S. Department of Transportation (DOT) in 1971. The study concluded that the tort system:

. . . ill serves the accident victim, the insuring public and society. It is inefficient, overly costly, incomplete and slow. It allocates benefits poorly, discourages rehabilitation and overburdens the courts and the legal system. Both on the record of its performance and the logic of its operation, it does little if anything to minimize crash losses.⁴

Recent studies by the RAND Institute for Civil Justice document that these problems remain today. These deficiencies define the reality of the tort and liability insurance system, which will remain drivers' only option in 37 states unless S. 837 is adopted.

The shortcomings of the tort system are the inevitable byproduct of a system which requires an injured person to jump through hoops to recover compensation. First, he must identify and show that the other driver was at fault. Second, the injured person must show that he was without fault or only partially at fault. Third, he must obtain a settlement or prevail in a lawsuit. Fourth, if he successfully makes it through the first three hoops, he can only recover his damages if the other person has sufficient insurance or other financial resources to pay for his loss. Finally, to add insult to injury, he has to pay his attorney about one-third of any recovery.

The Tort System Has Significant Compensation Gaps

A person injured in an automobile crash is not entitled to recover under the tort system unless he can establish that someone else was at least partially at fault. Thus, a person who crashes into a tree cannot recover. He cannot sue the tree. Such one-car accidents are the single

legislation, saying that: "No-fault systems have proven to be far more efficient in delivering benefits to the victims of automobile accidents than the current tort system, and they also provide greater opportunities to coordinate and reduce overall insurance costs. Too great a percentage of the premiums paid by policy-holders goes for the administration of the current wasteful tort liability system. No-fault would save money and court-time. It deserves Congressional support."

⁴ *Motor Vehicle Crash Losses and Their Compensation in the United States, A Report to the Congress and the President*, United States Department of Transportation (March 1971), 100. [Hereinafter, DOT]

largest category of cases where there is no compensation whatsoever under the tort system. In total, *30 percent of all auto accident victims recover nothing* under the tort system.⁵

People with No Injuries or Minor Ones Receive Far More than their Economic Losses
While the Seriously Injured Receive Inadequate Compensation for their Losses

For those fortunate enough to be able to recover under the tort system, the pattern of recovery is perverse. Chart 1 demonstrates that people with minor injuries are vastly overcompensated, while the seriously injured, on average, recover only a small fraction of their medical bills and lost wages and nothing for pain and suffering.

There are two reasons for high recoveries for small injuries under the tort system. First, lawyers know the value of a nuisance suit for small or feigned injuries. Plaintiffs, with the encouragement of their lawyers, submit inflated claims for injuries and sometimes even claims for nonexistent injuries in order to build up medical costs to increase their recoveries. Attorneys know insurers will settle these small claims because it is cheaper to settle than to pay their attorneys to fight it out in court. Second, because of the difficulty of quantifying nonmonetary losses, pain and suffering awards are typically calculated simply by tripling the amount paid for medical bills and lost wages. When an attorney knows the other driver has enough insurance to cover the claim, an attorney can encourage the injured person to run up medical bills in order to hit the pain and suffering jackpot. As a result, *people with economic losses up to \$2,000 recover, on average, about two and a half times their losses.*⁶

The greatest shame of the current tort system is the treatment of the seriously injured, such as those with permanent and total disability. The primary reason for inadequate recovery is the policy limits of the other driver's coverage. While some people carry higher limits of insurance, many are uninsured or underinsured. About 15 percent of all American drivers have no auto insurance coverage,⁷ with the figure as high as 30 percent in some states. Many other motorists carry only the minimum amounts of liability insurance needed to meet state law, about \$15,000 to \$20,000, and many more carry levels that are well below the amounts needed to compensate a seriously injured victim. Overall, the "average" motorist has about \$60,000 of liability insurance to pay for the losses of an injured person in an accident.

As a result, *an injured person with medical expenses and lost wages between \$25,000 and \$100,000 recovers on average only 56 percent of those losses and nothing for pain and suffering. For persons with catastrophic injuries and losses of over \$100,000, average recovery*

⁵ Steven J. Carroll, Allan F. Abrahamse, *The Effects of a Choice Automobile Insurance Plan on Insurance Costs and Compensation, An Updated Analysis* (Santa Monica, CA: RAND Institute for Civil Justice, 1998), 11 at footnote 9. [Hereinafter, Carroll and Abrahamse]

⁶ Stephen Carroll, James Kakalik, Nicholas Pace, John Adams, *No-Fault Approaches to Compensating People Injured in Automobile Accidents* (Santa Monica, CA: RAND Institute for Civil Justice, 1991), 21-22. [Hereinafter, Carroll, Kakalik, Pace and Adams].

⁷ Carroll and Abrahamse, *supra* note 3 at 13, footnote 16.

*drops to 9 percent.*⁸ Those figures represent the plaintiff's gross recovery, before his attorney takes one-third or more of the recovery, no matter how simple the case.

The Tort System is Slow to Pay Injured Persons

The need to establish fault under the tort system slows the receipt of compensation. The DOT study found that it took 19 months to receive payment in serious injury cases.⁹ In areas with crowded court dockets, the wait is measured in years. The delay in payment puts pressure on the seriously injured, particularly the poor, to settle their claims for less than they are worth.

The only money auto insurance provides in the interim is a few thousand dollars for those who have medical payments coverage, the only part of the personal injury portion of the premium that pays benefits without regard to fault. Of course, people who are fortunate enough to have -- and pay for -- health insurance, another non-fault-based coverage, can recover quickly. The necessity for health insurance -- both private and public -- to pick up much of the costs of auto accident victims significantly and unnecessarily increases the cost of health insurance.

The Tort System Pays Too Many Dollars to Lawyers and Too Few to Injured Persons

A system that requires lawyers and courts to adjudicate fault will always be an expensive, inefficient means for compensating accident victims. Contingency fee attorneys are usually paid about one-third of an injured person's recovery as a fee. Attorneys for insurers are paid on an hourly basis. As a result, as Chart 2 reveals, more than 28 cents out of every premium dollar drivers pay for bodily injury liability and uninsured motorist coverage goes to attorneys. That is almost twice the 14.5 cents that are paid to victims for legitimate medical bills and lost wages.

Massive Insurance Fraud Raises Premiums for All Drivers

Fraud -- from staged accidents to the filing of claims for nonexistent injuries and the routine padding of medical bills -- has driven insurance rates sky high, hitting most cruelly at the poorest members of our society. The problems have worsened over the last quarter of a century.

The incentive for the fraud is the tort system. First, damages are awarded for all of the medical bills and wage losses of a person injured in a car crash, without regard to whether that person has already received compensation for the losses from other sources, such as health insurance. This provides an incentive for people to run up their medical bills because they often can be paid twice for the same bills.

Second, injured persons receive compensation for their noneconomic damages, such as pain and suffering. Because it is difficult, if not impossible, to quantify these losses, noneconomic damage awards are typically calculated as a multiple of economic losses -- usually three times.

⁸ Carroll, Kakalik, Pace and Adams, *supra* note 4 at 21-22.

⁹ DOT, 43.

Under antitrust law, willful wrongful conduct results in trebled awards. Under tort law, conduct that Senator Moynihan has characterized as “statistically predictable collisions -- foreseeable events -- in a complex transportation system such as the one we have built”¹⁰ often results in quadrupled awards. The path to maximum recovery under the tort system is obvious -- run up medical bills, necessary or not, because they are, in effect, quadrupled.

The results are predictable -- both staged fraud and the everyday padding of bills. FBI Director Louis Freeh has estimated that every American household is burdened by an additional \$200 in unnecessary insurance premiums to cover the cost of staged accidents and the attendant massive fraud in the health care system. Sadly, some staged accidents have resulted in serious injuries and death.

Although less dramatic, the daily filing of excessive claims is even more costly. People injured in California, a fault jurisdiction, have about 250 soft-tissue injuries (sprains, strains, pains and whiplash) to 100 verifiable “hard” injuries (such as broken bones). In sharp contrast, people in Michigan,¹¹ a good no-fault insurance state, have about 70 soft-tissue injuries for every 100 hard injuries. The reason for the difference is that in Michigan there is little incentive to run up medical bills because you are only paid once for those bills.¹² With little incentive to file false claims or to build up claims, the lower filing level approximates the true injury level. It is interesting to note that the 18 states with the highest ratio of soft-tissue to hard injury claims are all tort states.¹³

What is the cost of these excess claims? A 1995 RAND Institute for Civil Justice study estimated that 35 to 42 percent of medical claims filed were excessive. RAND estimated that “excess consumption of health care in the auto arena *in response to tort incentives* accounted for about \$4 billion.”[emphasis added] Noneconomic and other losses from excessive claiming behavior cost another \$9-13 billion. The total bill to driving consumers was some \$13 to \$18 billion.¹⁴ These excess claims also raise the costs of private health insurance, Medicare and Medicaid.

¹⁰ Statement of Senator Daniel Patrick Moynihan accompanying introduction of S. 837, *Congressional Record* (April 20, 1999), S3924.

¹¹ Stephen Carroll, Allan Abrahamse and Mary Vaiana, *The Costs of Excess Medical Claims for Automobile Passenger Injuries* (Santa Monica, CA: RAND Institute for Civil Justice, 1995), 13. [Hereinafter, Carroll, Abrahamse and Vaiana]

¹² Michigan law permits injured people to sue for noneconomic damages but only in cases of serious or permanent injuries. Michigan’s threshold reduces the incentive of injured people to inflate medical bills because the right to sue is contingent on the nature of the injury, not the amount of the medical bills. Even in Michigan, some people inflate their medical bills in an effort to cross the threshold.

¹³ Carroll, Abrahamse and Vaiana, *supra* note 9 at 14.

¹⁴ Carroll, Abrahamse and Vaiana, *supra* note 9 at 23.

Chart 2 shows that the amount of fraudulent and excessive claims -- 12.6 percent of the bodily injury premiums in tort states -- nearly equals the amount paid for legitimate medical bills and lost wages, 14.5 percent.

STATE EXPERIENCE WITH NO-FAULT AUTOMOBILE INSURANCE IDENTIFIES THE PATH TO BETTER AUTO INSURANCE COVERAGE

It is 28 years since the first no-fault insurance law, authored by Michael Dukakis, went into effect in Massachusetts. Today 13 states have some form of no-fault insurance¹⁵ and they have accomplished their role as laboratories of auto insurance reform. We now know what combination of benefits and restrictions on lawsuits works best to lower premiums and provide better protection for accident victims.

The state experience with no-fault or first party, non-fault-based auto insurance was not a radical departure in the law. Most insurance in the United States is first party, non-fault-based insurance in the sense that a person's own insurer pays benefits based on the occurrence of an insurable event rather than a determination of fault. All health insurance, including Medicare, is first party insurance. When an elderly woman has treatment for a fractured hip, Medicare does not first make her prove that someone else was "at fault." It pays her bill, no questions asked.

Homeowners coverage is another form of first party insurance. So is workers' compensation. Neither of these coverages forces an injured person to engage in a costly and pointless exercise to find that someone else was at fault before compensation for losses is paid. Even most kinds of coverage under an automobile insurance policy in a tort state are first party -- "collision" for damage to the car and "comprehensive" for other damage such as fire and theft. First party insurance should be extended to the personal injury portion of automobile insurance.

First party, non-fault-based automobile insurance is simple and inexpensive. People give up an uncertain opportunity to recover inadequate compensation for serious injuries, slowly, under the tort system. In return, they receive an assured right, in all cases, to receive prompt payment for their economic losses, up to the limits they choose for themselves and their families. Under S. 837, they can also sue an at-fault driver for any economic losses above their policy limits. More people can be paid more dollars for a lower premium because the tort incentives to file fraudulent claims disappear, because attorneys and their fees are no longer needed as a predicate to compensation and because overpayment of small claims is eliminated. In short, *first*

¹⁵ No-fault automobile insurance is a form of insurance that combines first party benefits, paid by one's own insurer for economic loss without the necessity of proving fault, with some restrictions on lawsuits. The following states have laws that both provide for the payment of first party benefits and contain some form of restrictions on lawsuits for noneconomic damages: Colorado, Florida, Hawaii, Kansas, Kentucky, Massachusetts, Michigan, Minnesota, New Jersey, New York, North Dakota, Pennsylvania and Utah.

party auto insurance replaces the right to sue with the right to recover.

State No-Fault Insurance Laws Provide Faster and Better Compensation

How has first party insurance worked at the State level? Twenty-eight years of experience echoes the conclusion of a 1977 U. S. Department of Transportation (DOT) study that “State no-fault plans . . . provide more adequate and equitable benefits than the tort liability system.”¹⁶ A follow-up DOT study in 1985 found that: “Significantly more motor vehicle accident victims receive auto insurance compensation in no-fault states than in other States; . . . compensation payments under no-fault insurance are made far more swiftly than under traditional auto insurance; [and] . . . no-fault insurance systems pay a greater percentage of premium income to injured claimants than do traditional liability systems.”¹⁷

It was the deficiencies of the tort and liability insurance system, combined with the success of the Michigan no-fault law in addressing these faults, that led Senators Phil Hart, Warren Magnuson, Ted Stevens and Daniel Inouye to champion federal standards no-fault auto insurance reform in the 1970s. That legislation would have required all states to implement federal no-fault standards. John Martin, testifying on behalf of the AARP in 1977, said that the AARP is “convinced that the principal of no-fault automobile insurance is sound and that it will result in better benefits and prompt payments as opposed to the operations of the tort liability system with its delays and consumption of premiums and fees and litigation costs.”¹⁸

State No-Fault Laws’ Cost Savings Have Been Undermined by the Trial Bar

Despite the benefits of first party insurance and broad early consumer support, only 13 states have no-fault laws today. No state has enacted a law since 1976.¹⁹ While no-fault has delivered on its promises of fast and better compensation for all, many of the State laws have failed to deliver on the promise of lower premiums.

The basic problem with these state no-fault laws is that they permit too many lawsuits. As a result of the power of the trial bar’s opposition, the restrictions on lawsuits have been weakened to the point where they are insufficient to offset the additional cost of no-fault benefits. Of course, they are more expensive.

¹⁶ *State No-Fault Automobile Insurance Experience, 1971 - 1977*, United States Department of Transportation (June 1977), 78.

¹⁷ *Compensating Auto Accident Victims*, United States Department of Transportation, (May 1985), 3-4.

¹⁸ Hearings before the Subcommittee on Consumer Protection and Finance of the Committee on Interstate and Foreign Commerce, House of Representatives, *Federal Standards for No-fault Motor Vehicle Accident Benefits Act* (1977), 537.

¹⁹ In the 1970s, 16 states adopted no-fault laws. Nevada, Georgia and Connecticut subsequently repealed them. Pennsylvania repealed its law in 1984 but adopted a “freedom of choice” law in 1990. Many states have modified their no-fault systems in the intervening years.

Eight of the laws rely on “dollar” thresholds that permit suits for pain and suffering when a person incurs \$2000 or so of medical expenses. These thresholds are easily breached, particularly with the encouragement of plaintiffs’ lawyers, so that the essential trade-off of no-fault auto insurance -- prompt and certain compensation for economic losses for all injured people in exchange for restrictions on the legal lottery system -- is gutted.

Dollar thresholds often produce the most expensive of all worlds -- a no-fault system on top of a barely restrained tort system. Dollar thresholds in most states are targets, giving the unscrupulous even greater incentives to file fraudulent claims than under the tort system.

It is the height of hypocrisy for those who have worked hardest to weaken thresholds and then taken advantage of the loopholes they have created to increase the costs of the system to now turn around and argue that S. 837 is just another no-fault bill that should be rejected because the state no-fault experiments have failed to keep costs down. To the contrary, S. 837 is a choice bill and the state data and RAND cost estimates show that a predominantly first-party insurance system with tight restrictions on lawsuits will eliminate a huge amount of fraud and, therefore, lower premiums significantly.

S. 837: A PRESCRIPTION FOR LOWER PREMIUMS, BETTER BENEFITS AND MORE CONSUMER CHOICE

What we have learned from nearly 100 years of experience with the tort and liability insurance system is that it cannot be repaired. Changes are costly and do not address gaps in compensation and slow payments. The only consistent winners under the tort and liability insurance system, regardless of how modified, are lawyers and the providers of unnecessary medical services.

By contrast, 28 years of state experience with no-fault auto insurance shows what works and what does not. All of those laws provide timely benefits to injured persons. They pay all injured persons. They all provide better compensation for more serious injuries. In these fundamental respects, they all are better than the tort system.

The record on costs is different. Dollar thresholds do not work in states with aggressive trial bars. They simply provide a target for the unscrupulous. The result is that all motorists pay higher premiums for the dishonesty of some. It is important, however, to reemphasize that the responsibility for the failure of some no-fault laws to lower costs lies not with the proponents of no-fault, but with the trial bar. When they could not stop the adoption of no-fault laws, the trial bar weakened them by encouraging dollar thresholds. Then, they exploited them.

Tight verbal thresholds do reduce the number of lawsuits enough to enable people to receive high levels of no-fault benefits for a somewhat lower premium. However, they do not address the problems of the poor, who can no more afford the Lincoln Town Car of insurance than they can afford to own a Lincoln Town Car. The poor need the option of a low cost product, even if it means lower benefits than wealthy people can afford.

The state experience provides a road map for both better benefits and lower premiums.

The key to achieving these goals is the elimination of all lawsuits except those for any excess economic loss. Unlike any state law, S. 837 offers drivers the right to purchase such insurance. And, it does not require drivers to carry such coverage -- it permits them to select it if they wish.

A Right to Consumer Choice Under S. 837

S. 837 builds upon the experience of the states, but it is unlike any state auto insurance reform law. It is also not the comprehensive federal standards bill supported by this Committee 25 years ago and favored by then-Governor Reagan and President Carter. It is not a one-size fits all bill: it does not require motorists to buy one form of coverage and it does not set coverage minimums beyond the ability of some people to afford. It does not prevent states from opting out of the system and it creates no federal bureaucracy.

Instead, it is legislation that maximizes individual choice by permitting drivers an option they do not have now -- to buy low cost insurance that provides accident victims with better, speedier compensation for their injuries.

It would not eliminate the tort system. Instead, it would expand drivers' insurance options so that they could choose between either a modified version of the system that exists in their state today or the new personal injury protection (PIP) option.

The PIP Option: Better Coverage at a Far Lower Premium

Drivers who want to opt out of the lawsuit lottery can elect the new option -- PIP coverage for economic loss. They would be able to choose the level of PIP benefits they need and can afford, so long as they choose a level at least equal to the minimum amount of insurance required in their state. When they are injured, instead of having to prove fault, they would simply file claims for their losses directly with their own insurer. It would be similar to filing a claim with a health or workers' compensation insurer. The insurer would be obligated to pay them within 30 days and would be subject to significant penalties and attorneys' fees if they failed to pay legitimate claims.

Fault would not be abolished. If the PIP driver suffers a loss that exceeds his first party coverage, he would still be able to sue any at-fault driver for uncompensated economic loss. He could, in turn, be sued by other drivers for his fault, but only for uncompensated economic loss. Premiums would still be raised for drivers who cause accidents.

No matter what level of benefits a PIP insured chose, she would receive better compensation than she receives today in the vast majority of serious injury cases. Contrast, for example, how Sue would be treated under the tort system and the PIP system if she suffers \$100,000 of injuries in an auto crash. In today's tort system, she would recover nothing from her tort coverage (and only about \$5,000 from her medical payments coverage) in the 30 percent of the cases where she cannot establish that the other driver was at fault. If she was "fortunate" enough to be hit by at-fault driver Joe, her recovery would depend upon the level of his coverage. If Joe carried the average amount of coverage, about \$60,000, she would get a net recovery from him of about \$40,000 (after paying her attorney's fee), plus another \$5,000 from her own medical payments coverage.

Under S. 837, if Sue chose the PIP option and selected the minimum amount of required benefits, about \$20,000, she would recover at least \$20,000, regardless of how the accident occurred. If the other driver was at fault, she would get her \$20,000 of PIP benefits from her own insurer plus \$60,000 from the other driver for uncompensated economic loss. She would be far better off for about half the premium cost.

Sue's compensation would be even greater if she could afford to forgo the cost savings and, instead, purchase the maximum amount of PIP benefits for the same cost. Then she would receive about \$300,000 of benefits for each member of her family -- and those benefits would be payable in any accident where such losses were incurred. Of course, all drivers would be free to determine the best balance of premiums and compensation to meet their families' particular needs.

The cost savings would be dramatic. According to a Joint Economic Committee (JEC) analysis of similar legislation in the 105th Congress, drivers who elect the PIP option would see an average 24 percent reduction in their overall auto insurance premium. For the bodily injury portion of the premium, the only part affected by this legislation, the average reduction would be 45 percent. The JEC estimates that the waste in the current system is so great that the overall annual reduction would be \$35 billion if all drivers elected the PIP option.²⁰ State no-fault insurance experience confirms that if lawsuits for pain and suffering -- the major cause of mediocre cost experience in some no-fault states -- are eliminated, there will be significant decreases in premiums.

This combination of better compensation for serious injuries and lower premiums is not a magic trick. It is accomplished by eliminating the fraud associated with the tort system's incentives, unnecessary attorneys' fees and pain and suffering (largely associated with minor injuries). Chart 3 compares the costs and benefits of the tort system with the PIP system.

Chart 3
Comparison of the Current Auto Liability Insurance System
versus
the Personal Injury Protection (PIP) System of Auto Choice

Personal Protection Insurance System	Tort/Liability Insurance System
1.	1.
Pays no benefits to more than 30% of all accident victims (often the victims of single-car accidents).	Pays benefits to <u>all</u> accident victims.
2.	Pays benefits contingent on other driver's

²⁰ *Auto Choice: Impact on Cities and the Poor*, Joint Economic Committee, United States Congress (March 1998), 34-36.

fault.

3.

Eliminates the incentives of the tort/liability insurance system for fraud.

Makes recovery contingent on other driver's behavior and auto insurance coverage.

5.

Affords equitable coverage:

- All economic losses are compensated up to the level of coverage selected.
- Permits suits for excess economic losses.

In serious injury cases, pays for losses only after trial or settlement, which can take 2 to 3 years.

7.

Eliminates the need for most lawyers. Uses the savings to pay more injured people more equitably and to lower premiums.

Is unnecessarily expensive: \$400/year per car for average bodily injury premium, nationwide.

Pays benefits to all accident victims, regardless of fault.

Encourages fraud (more than one-third of all medical claims are fraudulent in response to the incentives of the tort/ liability insurance system).

4.

Allows each individual to determine the level of his or her own guaranteed benefits.

Provides inequitable coverage:

- Minor injuries are compensated at an average of 2 to 3 times economic losses.
- Serious injuries are compensated at an average of less than 50% of economic losses.

6.

In minor and serious injury cases, pays for insured losses within 30 days of submission of a bill.

Pays almost twice as many dollars for lawyers as for victims' legitimate medical bills and lost wages.

8.

Is affordable: \$216/year per car for personal injury protection benefits and residual bodily injury liability coverage.

Benefits of the PIP Option for Low Income People

The PIP option is of particular benefit to the poor. In some areas of the country today, poor people are faced with a Hobson's choice -- forgo basic necessities to pay for auto insurance or violate the law and drive without it. In testimony before this Committee last September, Professor Robert Lee Maril cited the results of his study of low income residents of Maricopa County, Arizona. He found that "the poorest households paid almost one-third of their total annual income for mandatory car insurance." In addition, he found that "low income households frequently were forced to put off purchases of basic necessities (such as food, rent and health care) to pay for mandatory car insurance."

Problems for low income people are compounded by the fact that many reside in major cities, where auto insurance is most expensive. With transportation a key factor in the effort to move people from welfare to work, it is a cruel reality that many people simply cannot afford the cost of insurance to own a car to get to a good paying job.

Denver Mayor Wellington Webb, in testimony in favor of Auto Choice before this Committee last Fall, explained this point well: "What does (Auto Choice) mean in human terms? It means that fewer of our working poor will be required to choose between groceries and auto insurance, and fewer middle-class Americans will be forced to choose between their retirement and their children's education."

How will the PIP option of S. 837 help low income people in general? The JEC study concludes that the low income drivers would see their premiums reduced by the most, an estimated 36 percent.²¹ PIP insurance is progressive insurance because its cost depends upon the potential loss of the insured. A poor person has a lower potential work loss and that lower potential can be reflected in significant cuts in premiums. As with all other drivers who elect the PIP option, the poor would also receive better benefits, on average, than they do today in the event of a serious injury.

Rights of Drivers Who Choose Not to Switch

S. 837 does not require motorists to have PIP insurance. People who prefer the present system in their state could choose a modified version of that system, one that would assure them greater likelihood of compensation in the event of an accident, for the same cost. Any person who elects this option would see no change in state law if he were involved in an accident with another driver who elected to stay under the same system.

The system would change only if he were involved in an accident with a PIP driver. In

²¹ *Auto Choice: Impact on Cities and the Poor*, Joint Economic Committee, United States Congress (March 1998), 35.

such a situation, the person would insure himself for both economic and noneconomic damages through “tort maintenance coverage” (TMC). This coverage operates just as uninsured motorist coverage operates today in a tort state. If the injured person can prove the other driver was at fault, then he can recover up to the limits of his own policy. The rules for determining liability would be governed by state law. Unlike uninsured motorist coverage, however, if he has any uncompensated economic loss, he can also sue the PIP driver on a fault basis for such losses. The TMC driver could not sue an at-fault PIP driver for noneconomic loss, with the important exceptions of accidents caused by alcohol or drugs. In turn, he could not be sued by a PIP driver except for excess economic damages.

A TMC insured would be more likely to receive *better* compensation for a serious injury under Auto Choice if he is injured by a PIP driver. That is because the injured person would now have two sources of recovery -- his own TMC coverage and the other driver’s insurance. Take, for example, a situation where Jeff suffers \$100,000 of economic losses in an accident. In a tort state today, if he were hit by a completely at-fault average driver, with \$60,000 of liability insurance coverage, he would net about \$40,000 (after paying his attorney). As a TMC electee under S. 837, he would collect \$60,000 from his TMC coverage,²² but then he could also sue the at-fault driver for \$40,000 of uncompensated loss. The result would be about twice the recovery of the tort system for a premium that RAND estimates will cost about the same as today.²³

State Options under Auto Choice

Not only does the bill give drivers options as to which system to choose and what level of benefits to purchase, S. 837 gives the states options as well. A state can simply choose to let the bill go into effect and give their drivers a choice. Alternatively, unlike most other federal legislation, the bill permits any state to pass legislation that would prevent the provisions of Auto Choice from applying in that state. S. 837 also provides that the law will not go into effect in a state if the state insurance commissioner determines that it would not lower the average bodily injury premium by at least 30 percent. Lastly, the bill permits states to opt out of Auto Choice even after it has been implemented -- be it one day or 50 years later.

In the last Congress, Michigan Governor John Engler cited these provisions approvingly, saying that, “Rather than forcing states to adopt a federal standard for automobile insurance, the Auto Choice Reform Act . . . allows states to opt out’ . . . without risking the loss of federal funds or other benefits.”

The Auto Choice Reform Act of 1999 expands state protections even beyond those provided in last Congress’ legislation. Unlike its predecessor, S. 837 affords each state up to one year to opt out of the new system before it would be implemented.

²²RAND assumes that TMC drivers will carry the same amount of TMC coverage as they carry bodily injury liability coverage.

²³Carroll and Abrahamse, *supra* note 2 at 19.

S. 837 Puts the Choice Where It Belongs -- with the Consumer

Mr. Chairman, our economy and our democracy depend upon people having the right to make choices. We decide not only what kind of clothes we will buy, what we will eat and where we will bank (with what kind of account), we decide what long distance telephone carrier to use, what mutual funds we will buy and what health care provider we will use.

Why should auto insurance be any different? Today's state insurance systems, with three exceptions, do not offer consumers any choice. Instead, they mandate one specific form of coverage. Four out of five times that mandate is the tort system, a system that encourages fraud and provides bad compensation at high prices.

S. 837 would offer consumers a better system, the PIP system, and then leave it up to individual drivers to decide between it and a modified version of the system now in place in their state.

CAR believes the choice system in S. 837 would be better for individuals and better for society. CAR strongly urges the Committee to report S. 837 expeditiously and let drivers decide the best form of insurance for themselves and their families.